

**REPORT OF THE AUDITOR-GENERAL TO THE NORTH WEST PROVINCIAL LEGISLATURE  
AND THE COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE  
INFORMATION OF THE TLOKWE CITY COUNCIL FOR THE YEAR ENDED 30 JUNE 2008**

**REPORT ON THE FINANCIAL STATEMENTS**

**Introduction**

1. I was engaged to audit the accompanying financial statements of the Tlokwe City Council which comprise the statement of financial position as at 30 June 2008, statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory notes, as set out on pages XX to XX.

**Responsibility of the accounting officer for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the basis of accounting determined by the National Treasury, as set out in accounting policy note 1 and in the manner required by the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2007 (Act No. 1 of 2007) (DoRA). This responsibility includes:
  - designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
  - selecting and applying appropriate accounting policies
  - making accounting estimates that are reasonable in the circumstances.

**Responsibility of the Auditor-General**

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on these financial statements based on conducting the audit in accordance with the International Standards on Auditing and *General Notice 616 of 2008, issued in Government Gazette No. 31057 of 15 May 2008*. Because of the matters discussed in the Basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.
4. Paragraph 11 *et seq.* of the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of Financial Statements* requires that financial reporting by entities shall provide information on whether resources were obtained and used in accordance with the legally adopted budget. As the budget reporting standard is not effective for this financial year, I have determined that my audit of any disclosures made by the Bojanala Platinum District Municipality in this respect will be limited to reporting on non-compliance with this disclosure requirement.

**Basis of accounting**

5. The municipality's policy is to prepare financial statements on the basis of accounting determined by the National Treasury, as set out in accounting policy note 1.

## **Basis for disclaimer of opinion**

### **Statement of Changes in Net Assets**

6. The previous year payments of R6 639 312 debited directly against the accumulated surplus in the Statement of Changes in Net Assets, is incorrect and should have been accounted for as follows:
  - Previous year expenditure of R1 868 674 should have been treated as a correction of a prior year error in terms of GRAP 3 *Accounting policies, changes in accounting estimates and errors*. This resulted in the comparative figures for creditors and general expenditure being understated.
  - Current year expenditure of R4 770 638 should have been accounted in the Statement of Financial Performance. This resulted in depreciation being understated by R4 915 639 and general expenses being overstated by R145 001.
7. I was unable to obtain sufficient appropriate audit evidence for the “Correction of error” of R120 592 913 disclosed in the Statement of Changes in Net Assets due to the inability of management to provide supporting documentation. The municipality’s records did not permit the application of alternative audit procedures. Consequently, I was unable to determine the valuation and allocation and completeness of the Accumulated Surplus, the Capitalisation Reserve, the Government Grant Reserve and the Donations and Public Contributions Reserve as disclosed in the Statement of Financial Position.
8. The contribution for depreciation of R16 999 410 from the reserves was not allocated to the Accumulated Surplus as required in terms of the accounting policies of these reserves. Management could however not disclose the account where this contribution was transacted to. This resulted in the Accumulated Surplus being understated and the undisclosed account being overstated with R16 999 410.

### **Reserves**

9. The combined carrying value of property, plant and equipment of R250 583 751 financed by the Government Grant Reserve and the Capitalisation Reserve as per the asset register, differed with the combined balance of R239 963 867 of these reserves as disclosed in the Statement of Changes in Net Assets. The difference of R10 619 884 could not be substantiated. The municipality’s accounting records did not permit alternative procedures to be performed. Consequently, I was unable to determine the valuation and allocation and completeness of the Government Grant Reserve and the Capitalisation Reserve as disclosed in the Statement of Financial Position.
10. Contrary to accounting policy 6.2, the municipality has, since conversion to GAMAP/GRAP, persisted to transfer new assets purchased from the Capital Replacement Reserve to the Capitalisation Reserve instead of to the Accumulated Surplus. This resulted in the Capitalisation Reserve being overstated and the Accumulated Surplus being understated by R70 147 509.
11. In terms of accounting policy 6.5, a Self Insurance Reserve was established to offset potential losses or claims that are not fully insured externally. The accounting policy further requires that the balance of this reserve should be based on the estimated insurance risk profile of the municipality. Management could however not provide the calculation of the estimated insurance risk done during the year under review. Consequently, I was unable to determine the valuation and allocation and completeness of the balance of R3 887 527 of this Reserve as at 30 June 2008.

## **Property, Plant and Equipment**

12. I was unable to obtain sufficient appropriate audit evidence for property plant and equipment with a carrying value of R295 283 005 disclosed in note 9.1 to the financial statements, due to inadequate information in the asset register regarding the descriptions, location and unbundling of property, plant and equipment as required by GAMAP 17 (Property, plant and equipment). The municipality's records did not permit the application of alternative audit procedures regarding these assets. Consequently, I did not obtain all the information and audit evidence I considered necessary to establish the rights and obligations, valuation and allocation, existence and completeness of property, plant and equipment.
13. In terms of accounting policy 7.1, the municipality elected to re-value its land and buildings. Land and buildings were however disclosed at cost less depreciation with a carrying value of R37 734 505. As it was impracticable to apply alternative procedures to quantify the possible effects on the financial statements, I was unable to determine the valuation and allocation of land and buildings included in property plant and equipment of R295 283 005 disclosed in note 9.1 to the financial statements.

## **Provisions**

14. The basis of calculation used to determine the provision for rehabilitation of refuse landfill-site of R2 494 404 as disclosed in note 4 to the financial statements could not be produced by management. As it was impracticable to apply alternative procedures to quantify the possible effects on the financial statements, I was unable to determine the possible misstatement of the provision and the expenditure.
15. The disaster fund provision of R392 049 disclosed in note 4 to the financial statements does not meet the definition of a provision as per paragraph 18 of GAMAP 19 (Provisions, contingent liabilities and contingent assets). As a result, provisions is overstated by R392 049, expenditure is overstated by R192 049 (being the current year provision) and accumulated surplus is understated by R200 000 (being the prior year provision).

## **Creditors**

16. I was unable to obtain sufficient appropriate audit evidence for suspense accounts of R10 961 969 disclosed in note 7 of the financial statements, due to the inability of management to provide supporting documentation. The municipality's records did not permit the application of alternative audit procedures. Consequently, I was unable to determine the valuation and allocation, rights and obligation, existence and completeness of these suspense accounts.

## **Consumer debtors**

17. Management did not consider the impairment of consumer debtors based on paragraphs 58 and 59 of IAS 39 (AC 133): *Financial instruments: Recognition and measurement*. Based on the results of audit procedures performed, debtors 90 days and older of R92 587 079 is deemed irrecoverable and needs to be impaired. The current provision of R58 214 907 for bad debts is thus understated by R34 372 172, resulting in consumer debtors and the surplus for the year both being overstated by R34 372 172.
18. Consumer debtors with credit balances of R1 260 534 were added back twice to the debtors balance as disclosed in note 14 to the financial statements. This resulted in both consumer debtors in note 14 and creditors in note 7 to the financial statements being overstated by R1 260 534.

## **Inventory**

19. The difference of R979 176 between inventory as disclosed in note 13 to the financial statements and the inventory listing was due to stock shortages found during the annual stock count. This resulted in both inventory and the accumulated surplus being overstated by R979 176.

## **Revenue**

20. GAMAP 9: *Revenue* determines that a conditional government grant is only recognised as revenue when there is compliance with the conditions attached to it. As disclosed in notes 19.1 to 19.20 to the financial statements, the government grants for which conditions were met during the year amounted to R43 735 129, whilst only an amount of R28 810 361 was disclosed as revenue in note 19 to the financial statements. This resulted in both revenue and expenditure in the Statement of Financial Performance being understated by R14 924 768.
21. I was unable to obtain sufficient appropriate audit evidence for interest of R2 293 185, received on external investments, included in the total interest received of R13 907 021 disclosed in note 37 to the financial statements, due to the inability of management to provide supporting documentation. The municipality's records did not permit the application of alternative audit procedures. Consequently, I was unable to determine the occurrence, accuracy, cut-off and completeness of interest received of R13 907 021 disclosed in note 37 to the financial statements.

## **Employee related cost**

22. I was unable to obtain sufficient appropriate audit evidence for employee related costs of R13 901 369 included in total employee related costs of R125 112 325 disclosed in note 21 to the financial statements, due to employee files not being available for audit and a limitation imposed by circumstance on the physical verification of employees. The municipality's records did not permit the application of alternative audit procedures.
23. A deduction of R2 364 709 from employee related costs disclosed in note 21 to the financial statements could not be explained by management. The municipality's records did not permit the application of alternative audit procedures.
24. Consequently, I was unable to obtain sufficient appropriate audit evidence to determine the occurrence, accuracy and completeness of employee related costs of R125 112 325 disclosed in the statement of financial performance.

## **Unauthorised Expenditure**

25. Contrary to section 125(2)(d) of the MFMA, the municipality incurred the following unauthorised expenditure, which was not disclosed in the financial statements:
  - Expenditure of R1 644 586 incurred for assets that were either not budgeted for or which exceeded the approved budget.
  - The operating budgets of the Office of the Executive Mayor, the Office of the Speaker and Corporate Services were overspent by a total of R5 027 076.

## **Disclaimer of opinion**

26. Because of the significance of the matters described in the basis for disclaimer of opinion paragraphs, I have been unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements of the Tlokwe City Council. Accordingly, I do not express an opinion on the financial statements.

## OTHER MATTERS

I draw attention to the following matters that relate to my responsibilities in the audit of the financial statements:

### Internal controls

27. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes that gave rise to the inefficiencies in the system of internal control, which led to the disclaimer of opinion. The root causes are categorised according to the five components of an effective system of internal control. In some instances deficiencies exist in more than one internal control component.

Reporting item	Control environment	Risk assessment	Control activities	Information and communication	Monitoring
Statement of Changes in Net Assets	X	X	X	X	X
Reserves	X	X	X	X	X
Property, plant and equipment	X	X	X	X	X
Provisions	X	X	X		X
Creditors	X		X		X
Consumer debtors	X		X		X
Inventory	X		X		X
Revenue	X		X		X
Employee related cost	X		X		X
Unauthorised expenditure	X		X		X
<p><u>Control environment</u>: establishes the foundation for the internal control system by providing fundamental discipline and structure for financial reporting.</p> <p><u>Risk assessment</u>: involves the identification and analysis by management of relevant financial reporting risks to achieve predetermined financial reporting objectives.</p> <p><u>Control activities</u>: policies, procedures and practices that ensure that management's financial reporting objectives are achieved and financial reporting risk mitigation strategies are carried out.</p> <p><u>Information and communication</u>: supports all other control components by communicating control responsibilities for financial reporting to employees and by providing financial reporting information in a form and time frame that allows people to carry out their financial reporting duties.</p> <p><u>Monitoring</u>: covers external oversight of internal controls over financial reporting by management or other parties outside the process; or the application of independent methodologies, like customised procedures or standard checklists, by employees within a process.</p>					

### Non-compliance with applicable legislation

#### 28. MFMA

- Contrary to section 32, the accounting officer did not action unauthorised expenditure.
- Contrary to section 62, no risk assessment was performed in the period under review.
- Contrary to section 63(2)(a), the fixed asset register was not properly maintained.
- Contrary to section 167(2), sufficient appropriate audit evidence that the mayoral vehicle was only used for official trips, was not submitted for audit.

29. **Local Government: Municipal Systems Act, 2000 (Act No.32 of 2000)**
- Contrary to section 57, no performance agreement was signed with the accounting officer.
  - Contrary to section 57, two of the managers did not have valid employment contracts.
  - Contrary to section 104, council did not have a fraud prevention plan.
  - Contrary to paragraph 12A of schedule 1, two councillors had consumer accounts outstanding for longer than 90 days as disclosed in note 30.6 of the financial statements.
30. **Value Added Tax Act, 1991 (Act No. 89 of 1991)**
- Contrary to section 55 the municipality did not keep VAT records for 5 years.

#### **Matters of governance**

31. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of certain key governance responsibilities, which I have assessed as follows:

No.	Matter of governance	Yes	No
	<b>Audit committee</b>		
1(a)	The municipality had an audit committee in operation throughout the financial year.		X
1(b)	The audit committee operates in accordance with approved written terms of reference.		X
1(c)	The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA.		X
	<b>Internal audit</b>		
2(a)	The municipality had an internal audit function in operation throughout the financial year.		X
2(b)	The internal audit function operates in terms of an approved internal audit plan.		X
2(c)	The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA.		X
	<b>Other matters of governance</b>		
3	The annual financial statements were submitted for audit as per the legislated deadlines in Section 126 of the MFMA.	X	
4	The annual report was submitted for the auditor for consideration prior to the date of the auditor's report.	X	
5	The financial statements submitted for audit were not subject to any material amendments resulting from the audit.		X
6	No significant difficulties were experienced during the audit concerning delays or the unavailability of expected information and/or the unavailability of senior management.		X
7	The prior year's external audit recommendations have been substantially implemented.		X
8	The Provincial SCOPA resolutions have been substantially implemented.		X
	<b>Implementation of Standards of Generally Recognised Accounting Practice (GRAP)</b>		
9	The municipality submitted an implementation plan, detailing progress towards full compliance with GRAP, to the National Treasury and the relevant provincial treasury before 30 October 2007.	X	
10	The municipality substantially complied with the implementation plan it submitted to the National Treasury and the relevant provincial treasury before 30 October 2007, detailing its progress towards full compliance with GRAP.		X

No.	Matter of governance	Yes	No
11	The municipality submitted an implementation plan, detailing further progress towards full compliance with GRAP, to the National Treasury and the relevant provincial treasury before 31 March 2008.		X

### Unaudited supplementary schedules

32. The municipality provided supplementary information in the financial statements on whether resources were obtained and used in accordance with the legally adopted budget, in accordance with GRAP 1 *Presentation of Financial Statements*. The supplementary budget information set out on pages [xx] to [xx] does not form part of the financial statements and is presented as additional information. Accordingly I do not express an opinion thereon.

## OTHER REPORTING RESPONSIBILITIES

### REPORT ON PERFORMANCE INFORMATION

33. I was engaged to review the performance information.

#### Responsibility of the accounting officer for the performance information

34. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the MSA.

#### Responsibility of the Auditor-General

35. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008* and section 45 of the MSA.
36. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.
37. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

### Audit findings (performance information)

#### Non-compliance with regulatory requirements

38. Contrary to section 46 of the MSA and section 121(3)(c) of the MFMA, council did not prepare a performance report which reflects the municipality's and any service provider's performance during the financial year, provides a comparison with the targets and the performance in the previous financial year and measures that were or are to be taken to improve performance.

## APPRECIATION

39. The assistance rendered by the staff of the Tlokwe City Council during the audit is sincerely appreciated.

*Auditor General*

Pretoria

28 November 2008



AUDITOR - GENERAL